

VIII. Tax Information and Legal Issues



Tax Information

Income Tax Withholding

Federal and California statutes require income tax withholding on distributions from pension plans, annuities and deferred compensation plans. Income tax will be withheld from the taxable portion of your allowance unless you take action *not* to have taxes withheld. To not have income tax withheld, you must file an Income Tax Withholding Preference Certificate with CalSTRS. This form is included in the service retirement application packet.

If you do *not* have taxes withheld or if you do not have enough withheld, you may need to make estimated tax payments. Generally, your withholding or estimated tax payments or the total of both must cover at least 90 percent of your total tax liability for the current year. Failure to meet the 90 percent limit could subject you to penalties.

A portion of your allowance or other benefit may not be taxable if you made previously taxed contributions to CalSTRS during your career. CalSTRS uses the Simplified General Rule established by the Internal Revenue Service to determine the taxable portion of your allowance. (You may use any acceptable method when reporting to the IRS.) The Simplified General Rule is explained in detail in *Pension and Annuity Income*, IRS publication 575, available from the IRS or in *Pension and Annuity Guidelines*, FTB publication 1005, from the state Franchise Tax Board or in *Notification of Income Tax Withholding*, MS 1357, from CalSTRS.

Periodic Payments

Unless you tell CalSTRS otherwise, CalSTRS will withhold income tax on your periodic payments (payments that are received in installments at regular intervals) as if you were married and claiming three dependents.

Non-Periodic Payments

CalSTRS withholds income tax from non-periodic payments (such as a lump-sum death payment or the allowance accrued and unpaid on the date of death of a CalSTRS benefit recipient) at a flat rate of 20 percent for federal and 6 percent for state withholding. Your beneficiary can elect not to have state taxes withheld from a nonperiodic payment unless he or she resides outside of the United States or its possessions, in which case, tax withholding is required. (Federal taxes must be withheld unless the payment was a rollover.)

Income Tax Withholding Preference Certificate (AD-0908)

If you wish to request a change to your income tax withholding status, you must complete CalSTRS form *Income Tax Withholding Preference Certificate*, AD-0908.

The form must be received by CalSTRS no later than the first day of the month preceding the month you wish the change to take effect. You may obtain an AD-0908 from CalSTRS by calling the CalSTRS automated telephone system at 800-228-5453 or by downloading the form from the CalSTRS Web site at www.calstrs.ca.gov.

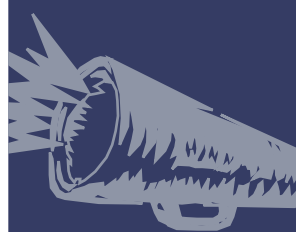
Lump-Sum Distributions

If you receive a lump-sum distribution, including a refund of your contributions, you should be aware that the Internal Revenue Code provides several complex rules regarding the taxation and penalties of such distributions. You may be eligible to defer tax liability on the taxable amount of the



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distribution by rolling over that amount into another qualified retirement plan or IRA.


To take advantage of these provisions, the distribution **MUST** be made by a trustee-to-trustee transfer. If you request a rollover distribution, additional information will be provided. Contact the CalSTRS Public Service Office at 800-228-5453 or 916-229-3870 for information regarding rollovers.

Source Tax

Pursuant to federal law, if you are *not* a resident of California, you are not subject to California state tax. However, CalSTRS benefits may be subject to taxation to the state in which you do reside.

CalSTRS will not withhold state income taxes for benefit recipients who live outside California *unless it is requested by filing an Income Tax Withholding Preference Certificate, AD 0908.*

CalSTRS recommends you consult a qualified tax professional for specific tax advice. You may contact the Internal Revenue Service, the California State Franchise Tax Board or a



qualified tax adviser for information relevant to your individual situation. For general information on withholding tax from CalSTRS benefit payments, call CalSTRS Teletalk at 800-228-5453 and request message #650.

Internal Revenue Code Section 401

Section 401 (a) (9) of the IRC and the California Education Code require CalSTRS to begin a distribution of a member's benefits no later than April 1 of the calendar year following the year the member reaches age 70 1/2.

CalSTRS will not begin distribution of your account if:

- you are currently employed in a position subject to coverage under the Teachers' Retirement Plan

- your current employment is covered by, or you are retired from, another public retirement system. For a listing of other public retirement systems, see Section XI, Glossary of Terms, Concurrent Retirement.

Annually, CalSTRS attempts to notify members who may be impacted by these statutory provisions. Therefore, it is important for members to ensure CalSTRS has a current mailing address for them at all times.

Note: The Internal Revenue Service may impose an excise tax equal to 50 percent of the minimum required distribution if the member receives less than the minimum-required distribution for a taxable year.

Internal Revenue Code Section 415

Section 415 of the IRC imposes a limit on benefits that can be paid by a state or local government defined benefit plan such as that administered by CalSTRS. Benefits are limited to an absolute dollar amount that is indexed for inflation. For 2001, the dollar limit is \$140,000, at ages 62 through 65. The limit is lower below these ages and higher above these ages.

Currently, few CalSTRS members have been, or are likely to be, affected by the limits of Section 415. CalSTRS will notify you, upon receipt of your application for retirement, if your benefit will be affected by the IRC Section 415 benefit limit. Pursuant to federal law, CalSTRS has established a Replacement Benefits Program from which benefits in excess of the Section 415 limits can be paid. If your benefit is limited by IRC Section 415, in addition to the limited benefit, you will receive a separate payment from the Replacement Benefits Program.

Legal Issues

Subrogation

When a third party causes the injury or death of a CalSTRS member before retirement and the member or family pursues civil litigation, CalSTRS must be informed. CalSTRS has a right to participate in the action to recover the expenses and

legal costs the injury or death generated. The process that permits this participation is called subrogation.

Power of Attorney

CalSTRS members can arrange for management of their assets, should they become incapacitated, through the use of a durable power of attorney. CalSTRS can provide you with some of the necessary forms.

When a CalSTRS benefit recipient becomes incapacitated and can no longer manage his or her financial affairs, CalSTRS may need to determine who has the legal authority to act on the recipient's behalf regarding the recipient's CalSTRS account and benefits. That authority could extend to changing the recipient's address, instituting or changing direct deposit authorizations and changing tax withholding preferences.

A durable power of attorney is the most common method used by a benefit recipient to delegate authority to act for the recipient. This document permits a benefit recipient to act as a principal and appoint an agent. The document also identifies the extent of authority granted to the agent.

A durable power of attorney can be drafted by an attorney or purchased as a commercially available fill-in-the-blank form. CalSTRS has a *Special Power of Attorney*, MS 1307, form available that may be used by a principal. The CalSTRS MS 1307 enables your named agent to handle all matters pertaining to a CalSTRS account, unless barred by law.

In addition, CalSTRS requires an agent to execute an affidavit affirming the agent's authority under the Durable Power of Attorney. For an agent's convenience, CalSTRS has a *Declaration of Attorney in Fact*, MS 1432, that can be completed by the agent each time the agent makes a request.

If you wish to obtain a *Special Power of Attorney*, MS 1307, or a *Declaration of Attorney in Fact*, MS 1432, call the

CalSTRS automated telephone system at 800-228-5453 or 916-229-3870 or download the form from www.calstrs.ca.gov.

Marriage Dissolution or Annulment and CalSTRS Benefits

If you have been divorced or are presently going through a divorce, there may be a community property interest in your CalSTRS benefits. You may need to refer to your Marital Settlement Agreement and/or contact an attorney for legal advice on how your benefits may be affected.

CalSTRS has *Community Property Information*, PAO-211, for members and their attorneys. To receive a copy of this booklet, contact the CalSTRS Public Service Office at 800-228-5453. The booklet can be seen online at www.calstrs.ca.gov in the Publications section.



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